

**TENNESSEE GENERAL ASSEMBLY  
FISCAL REVIEW COMMITTEE**



**CORRECTED  
FISCAL NOTE**

**HB 644 - SB 788**

March 27, 2013

**SUMMARY OF BILL:** Redefines “cost of doing business by the retailer” under the Unfair Cigarette Sales Law as fifteen percent of the basic cost of cigarettes to the retailer, rather than eight percent.

**ESTIMATED FISCAL IMPACT:**

On March 9, 2013, a corrected fiscal note was issued estimating a fiscal impact as follows:

(CORRECTED)

Decrease State Revenue – Net Impact – \$244,400/FY12-13  
\$1,466,600/FY13-14 and Subsequent Years

Increase Local Revenue – \$356,400/FY12-13  
\$2,138,400/FY13-14 and Subsequent Years

Due to an erroneous assumption, this impact was in error. This corrected fiscal note reflects the revised cigarette price elasticity of demand. The estimated fiscal impact is:

(CORRECTED)

Decrease State Revenue – Net Impact – \$23,800/FY12-13  
\$142,900/FY13-14 and Subsequent Years

Increase Local Revenue – \$389,400/FY12-13  
\$2,336,400/FY13-14 and Subsequent Years

Assumptions:

- Pursuant to Tenn. Code Ann. § 47-25-302(4), cost to the retailer is defined as the basic cost of cigarettes to the retailer plus the cost of doing business by the retailer.
- Pursuant to Tenn. Code Ann. § 47-25-303(a), it is a Class C misdemeanor for any retailer, with intent to injure competitors or destroy substantially or lessen competition, to advertise, offer to sell, or sell at retail, cigarettes at less than cost to the retailer.

**HB 644 - SB 788 (CORRECTED)**

- As a result, increasing the “cost of doing business by the retailer” will result in a higher price of cigarettes sold at retail.
- The average price per pack of 20 cigarettes in Tennessee is estimated to be \$5.00.
- According to the Department of Revenue, cigarette tax collections were approximately \$264,889,000 in FY11-12. Assuming negative growth of 0.6 percent in FY12-13 and 0.5 percent in FY13-14, cigarette tax collections in FY13-14 are assumed to be approximately \$261,983,168.
- Pursuant to Tenn. Code Ann. § 67-4-1004(a) and Tenn. Code Ann. § 67-4-1004(d)(1), cigarette tax is a \$0.62 tax per pack of 20 cigarettes.
- The total number of 20-pack cigarettes sold in FY13-14 is estimated to be 422,553,498 ( $\$261,983,168 / \$0.62$ ). This number is assumed to remain constant into perpetuity under current law.
- The basic cost of cigarettes to the retailer is estimated to be \$4.63 per 20-pack of cigarettes ( $\$5.00 / 108.0\%$ ). This number will remain unchanged as a result of this bill.
- Increasing the cost of doing business by the retailer, from eight to fifteen percent of the basic cost of cigarettes to the retailer, is estimated to result in a price increase for cigarettes to an average of \$5.32 per 20-pack [ $\$4.63 + (\$4.63 \times 15.0\%)$ ] for the consumer.
- This represents a 6.4 percent increase in the price of cigarettes sold to the consumer per each 20-pack [ $(\$5.32 - \$5.00) / \$5.00 \times 100$ ]. The increase in price of cigarettes will result in a decrease in the consumption of cigarettes.
- Based on various studies, the price elasticity of demand for cigarettes is estimated to be negative 0.35. The 6.4 percent increase in the price of cigarettes is estimated to result in a 2.24 percent decrease in the quantity of cigarettes consumed ( $6.4\% \times -0.35$ ).
- The number of 20-pack cigarettes sold as a result of this bill in FY13-14 is estimated to be 413,088,300 [ $422,553,498 \times (100.00\% - 2.24\%)$ ]. This number is assumed to remain constant into perpetuity.
- The total recurring decrease in state cigarette tax collections in FY13-14 and subsequent years is estimated to be \$5,868,422 [ $\$261,983,168 - (413,088,300 \times \$0.62)$ ].
- The current state sales tax rate is 7.0 percent; the average local option sales tax rate is estimated to be 2.5 percent.
- The total taxable sales of cigarettes is estimated to increase by \$84,862,266 as a result of this bill [ $(413,088,300 \times \$5.32) - (422,553,498 \times \$5.00)$ ].
- The recurring increase in state sales tax revenue beginning in FY13-14 is estimated to be \$5,940,359 ( $\$84,862,266 \times 7.0\%$ ); the recurring increase in local option sales tax revenue beginning in FY13-14 is estimated to be \$2,121,557 ( $\$84,862,266 \times 2.5\%$ ).
- Pursuant to Tenn. Code Ann. § 67-6-103(a)(3)(A), local governments receive 4.603 percent of state sales tax revenue as state-shared sales tax revenue.
- Pursuant to Tenn. Code Ann. § 67-6-103(q), no portion of revenue derived from the 0.5 percent sales tax rate increase, from 5.5 percent to 6.0 percent (effective April 1, 1992), or the 1.0 percent sales tax rate increase, from 6.0 percent to 7.0 percent (effective July 15, 2002), shall be distributed to local government.
- The effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 3.617% [ $(5.5\% / 7.0\%) \times 4.603\%$ ].

- The net recurring increase in state sales tax revenue beginning in FY13-14 is estimated to be \$5,725,496 [ $\$5,940,359 - (\$5,940,359 \times 3.617\%)$ ].
- The total recurring increase in sales tax revenue for local governments beginning in FY13-14 is estimated to be \$2,336,420 [ $\$2,121,557 + (\$5,940,359 \times 3.617\%)$ ].
- The net recurring decrease in state revenue beginning in FY13-14 is estimated to be \$142,926 ( $\$5,868,422 - \$5,725,496$ ).
- The bill will become effective on or before May 1, 2013. As a result, the first-year impact will be FY12-13. The first-year impact is estimated to be one-sixth of the full year impact.
- The net decrease in state revenue in FY12-13 is estimated to be \$23,821 ( $\$142,926 \times 1/6$ ).
- The total increase in local revenue in FY12-13 is estimated to be \$389,403 ( $\$2,336,420 \times 1/6$ ).

### **CERTIFICATION:**

The information contained herein is true and correct to the best of my knowledge.



Lucian D. Geise, Executive Director

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